

*United States Court of Appeals
for the Second Circuit*



APPENDIX

74-1510

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UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

SECURITIES AND EXCHANGE COMMISSION

Plaintiff

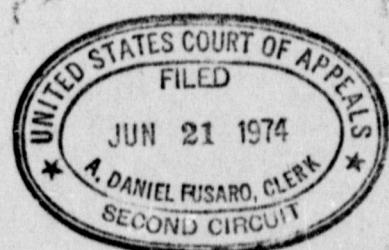
Case No; 74-1510
(T-3261)

-against-

JAMES JOSEPH HAMMARTH

Defendant

APPENDIX TO THE BRIEF



PAGINATION AS IN ORIGINAL COPY

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

SECURITIES AND EXCHANGE COMMISSION :
Plaintiff :
-against- :
JAMES JOSEPH HAMMARTH :
Defendant :

Case No:
74-1510
(T-3261)

APPENDIX TO THE BRIEF

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UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

-----x
SECURITIES AND EXCHANGE COMMISSION,

Plaintiff,

-against-

MIDLAND EQUITY CORPORATION,
JAMES JOSEPH HAMMARTH,

Defendants.

-----x
GAGLIARDI, D. J.

73 Civ. 2617

MEMORANDUM
DECISION

40100

The Securities and Exchange Commission moves this court for an order restraining the defendants, Midland Equity Corporation and James Hammarth the president, secretary and treasurer of Midland, from continued violations of the visitation and inspection provisions of the federal securities laws, specifically Section 17(a) of the Securities Exchange Act of 1934 (15 U.S.C. 578g(a)) and Rule 17a-4 promulgated thereunder (17 C.F.R. 240.17a-4).

The facts as presented in the affidavits submitted by the parties and as further developed at an evidentiary hearing before this court may be briefly summarized.

On October 25, 1972, in the course of an investigation into possible violations of the bookkeeping and net capital provisions of the federal securities laws by the defendants, S.E.C. compliance examiners George C. Appoldt and Robert Green visited Midland's offices at 180 Broadway, New York, New York. They discovered that the offices were locked and were apparently no

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*Carol
Sternberg
Paraskev*

(1) longer tenanted by Midland. The following day Appoldt and
Green located defendant Hammart at 160 Broadway. When they
requested to inspect Midland's books and records, Hammart
refused insisting that he was no longer a broker-dealer and
consequently not subject to N.A.S.D. or S.E.C. rules. Hammart
indicated that he based the conclusion that he was no longer a
broker-dealer on a letter received from the Securities Investor
Protection Corporation (S.I.P.C.) stating that Midland had
failed to pay its 1972 S.I.P.C. assessment. At the time of the
October 26, 1972 meeting Appoldt offered to provide Hammart
with the appropriate forms for withdrawal as a broker-dealer;
Hammart declined the offer.

(2) *Reserve*
Dealt with - 3.
The October 26, 1972 request to inspect the books and
records of Midland was reiterated in a letter mailed to Hammart
at both his business and residence addresses on January 31, 1973.
On May 17, 1973, Michael T. Gregg an S.E.C. staff attorney made
a final attempt to contact Hammart and obtain Midland's records.
Failing in this attempt, the S.E.C. instituted the instant action
for injunctive relief.

(3) *Action
for injunctive relief*
(4) Defendant Hammart's opposition to the instant motion
is two-fold. First, Hammart contends that as a result of its
failure to pay its 1972 S.I.P.C. assessment, Midland is no longer
a broker-dealer and therefore is not subject to the inspection
provision. Second, Hammart contends that as a result of a sale
of his Midland shares to one Joseph F. Goggins, he is not indiv-

(5) (1) —

(2) —

PY

individually subject to the inspection provision. We find both of these contentions equally untenable.

The procedures pursuant to which a registered broker-dealer may withdraw are explicitly set forth in Section 15(b)(6) of the Securities Exchange Act of 1934 [15 U.S.C. § 78o(b)(6)]. In order to terminate registration a broker-dealer is required to file a formal notice of withdrawal with the Commission; the form of such notice and the manner in which it must be filed are described in Rule 15b6-1 [17 C.F.R. 240.15b6-1]. Admittedly, ^{Midland Equity} ~~Hammarth~~ has never filed the required withdrawal form with the Commission. When S.E.C. compliance examiner Appoldt offered to supply Hammarth with copies of the appropriate withdrawal forms Hammarth refused. Current Commission records indicate Midland's continued status as a registered broker-dealer. In the face of these uncontested facts, Hammarth relies upon the theory that Midland's failure to pay its 1972 S.I.P.C. assessment in some manner effectuated a withdrawal of its registration as a broker-dealer. Essentially, Hammarth is arguing that Midland's failure to comply with the provisions of the Securities Investor Protection Act placed it beyond the reach of the S.E.C.'s power of inspection. This argument is clearly without merit.

Hammarth's contention that the purported sale to Goggins insulates him from the inspection provisions of the Act is not persuasive. At the hearing on this motion Hammarth announced that in February of 1972, approximately four months after the Commission's initial request to examine Midland's records, he

(8) sold his interest in Midland to one Joseph P. Goggins. Hammarth was unable to tell the court whether or not Goggins was currently in control of Midland. Moreover, Hammarth indicated that he was not willing to assist the Commission in locating Coggins and through him the books and records of Midland.

(9) Hammarth's attitude in response to questions concerning the purported sale can only be described as evasive and casts substantial doubt upon the bona fides of the sale. At the

(10) time of the sale Hammarth had violated and was continuing to violate the provisions of Section 17(a). His current attempt to frustrate the S.E.C.'s investigation by apparently divesting himself of control of Midland and placing its books and records in the hands of some unreachable third party does not relieve him of his responsibilities under the inspection provisions of the Act.

~~Only relationship was as an employee.~~
The action and the instant motion for a preliminary injunction seek judicial assistance in enforcing the provisions of section 17(a) of the Securities Exchange Act of 1934 and the rule promulgated thereunder. Section 17(a) provides in part that: ". . . every broker or dealer registered pursuant to section 15 . . . shall make, keep and preserve for such periods, such accounts, correspondence, memoranda, papers, books and other records, and make such reports, as the Commission by its rules and regulations may prescribe as necessary or appropriate in the public interest or for the protection of investors. Such accounts, correspondence, memoranda, papers, books and other records shall be subject at any

(5)

(1) time or from time to time to such reasonable periodic, special
& or other examinations. . . ." Rule 17-a⁽⁴⁾ provides that such
3 records shall be maintained for a period of 6 years and that in
4 the event a registered broker-dealer ceases to be registered he
5 shall maintain such records intact for the remainder of the time
6 period specified in the rule. The section and the rules promul-
7 gated thereunder are of undeniable importance in the enforcement
8 of the federal securities laws. In the absence of the power of
9 inspection afforded by these provisions, the Commission would
10 face substantial difficulties in its investigation of alleged
11 violations. See Fontaine v. Securities and Exchange Commission,
12 259 F. Supp. 130 (D. Puerto Rico 1966); Securities and Exchange
13 Commission v. Mainland Securities Corp., 192 F. Supp. 862 (S.D.
14 N.Y. 1961). In light of the importance of these sections and
in view of the defendant's past and continued violations, we
find that the Commission has made "a proper showing" of need for
injunctive relief under Section 21(e) of the Securities Exchange
Act of 1934 (15 U.S.C. §78u(e)) and accordingly the instant motion
is granted. Securities and Exchange Commission v. Broadwall Se-
curities Inc., 240 F. Supp. 962 (S.D.N.Y. 1965); Securities and
Exchange Commission v. General Securities Company, Inc., 216
F. Supp. 350 (S.D.N.Y. 1963).

*Post
vacation
continued
vacation*

Submit Order on ten days' notice.

U.S.D.J.

Dated: New York, New York
December 4, 1973.

P-7



UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
REGIONAL OFFICE
26 FEDERAL PLAZA
NEW YORK, N.Y. 10007

IN REPLYING PLEASE QUOTE

NY-E:MTG

May 3, 1974

Mr. James Joseph Hammarth
21 Davenport Avenue
New Rochelle, New York 10805

Re: SEC v. James Joseph Hammarth, Docket No.
74-1510 (T-3261)

Dear Mr. Hammarth:

I have been requested to inform you that Prof. Nathaniel Fensterstock, Staff Counsel, United States Court of Appeals, Second Circuit, has scheduled a pre-appeal conference for Tuesday, May 14, 1974 at 4:30 p.m. in Room 1804 of the United States Courthouse, Foley Square, New York, New York 10007.

You are, of course, permitted to attend with counsel if you desire but, in any event, your own attendance is required.

Very truly yours,

WILLIAM D. MORAN
Regional Administrator

by

Thomas R. Beirne
Thomas R. Beirne
Chief Attorney, Br. #3

cc:

Martin Berglas, Esq.
Office of General Counsel

P-8 Ref 19

INVESTOR PROTECTION CORPORATION
SUITE 2150
L'ENFANT PLAZA, S. W.
WASHINGTON, D. C. 20024



CERTIFIED
No. 717123

MAIL

SIPC

SECURITIES INVESTOR PROTECTION CORPORATION
485 L'ENFANT PLAZA, S.W. • SUITE 2150
WASHINGTON, D.C. 20024 • (202) 484-5400

2304-001L

Midland Equity Corporation
160 Broadway
New York NY 10038

OCT. 3 1972

Gentlemen:

Based upon the reports of your SIPC collection agent through September 2, 1972, our records indicate the following listed SIPC forms and assessment payments made, as well as apparent failure to file or pay, which should be compared with your records promptly:

	Filed	Amount Paid	Apparent Deficiency	
			Did not file	Other
Initial assessment (based on 1970 revenues)	✓	\$ 150 -		
1971 general assessment (Form SIPC-6)	✓	150 - <i>ppd.</i>		
1st Quarter				
2nd Quarter				
3rd Quarter				
4th Quarter				
1971 reconciliation (Form SIPC-7)			✓	
1972 general assessment (Form SIPC-6)			✓	
1st Quarter			✓	
2nd Quarter			✓	
Exclusion claimed (Form SIPC-3)				
1971				
1972				

Within ten days from the above date, will you please:

- a) Mail overdue form(s) together with any payment due to your SIPC collection agent, NASD, and
- b) Insert here the date _____ form(s) and payment in a) were mailed to your SIPC collection agent and the amount thereof \$ _____.
- c) If you disagree with the apparent deficiency(ies) above, send explanation to your SIPC collection agent.
- d) IN ADDITION TO a), b), AND c) ABOVE, RETURN ONE COPY OF THIS LETTER [AND A COPY OF ANY LETTER SENT TO YOUR COLLECTION AGENT PURSUANT TO c) ABOVE] TO SIPC IN THE ENCLOSED SELF-ADDRESSED ENVELOPE.

We wish to call to your attention Section 10 (a) of the Securities Investor Protection Act of 1970 which is quoted in part as follows:

"(A) FAILURE TO PAY ASSESSMENT, ETC. - IF A MEMBER OF SIPC SHALL FAIL TO FILE ANY REPORT OR INFORMATION REQUIRED PURSUANT TO THIS ACT, OR SHALL FAIL TO PAY WHEN DUE ALL OR ANY PART OF AN ASSESSMENT MADE UPON SUCH MEMBER PURSUANT TO THIS ACT, AND SUCH FAILURE SHALL NOT HAVE BEEN CURED, BY THE FILING OF SUCH REPORT OR INFORMATION OR BY THE MAKING OF SUCH PAYMENT, TOGETHER WITH INTEREST THEREON, WITHIN FIVE DAYS AFTER RECEIPT BY SUCH MEMBER OF WRITTEN NOTICE OF SUCH FAILURE GIVEN BY OR ON BEHALF OF SIPC, IT SHALL BE UNLAWFUL FOR SUCH MEMBER, UNLESS SPECIFICALLY AUTHORIZED BY THE COMMISSION, TO ENGAGE IN BUSINESS AS A BROKER OR DEALER. . ."

Very truly yours,

SECURITIES INVESTOR PROTECTION CORPORATION

Lloyd W. McChesney,
Lloyd W. McChesney
Vice President - Finance

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1 UNITED STATES DISTRICT COURT

2 SOUTHERN DISTRICT OF NEW YORK

4 -----X
4 SECURITIES AND EXCHANGE COMMISSION, :

5 Plaintiff, :

6 - against - :

7 MIDLAND EQUITY CORPORATION and :
8 JAMES JOSEPH HAMMARH, :

73 Civ. 2617

9 Defendants.

10 -----X
10 B e f o r e:

11 HON. LEE GAGLIARDI,

12 District Judge

14 New York, N. Y.
15 June 21, 1973

16 Appearances:

17 MICHAEL T. GREGG, Esq.
17 and
18 THOMAS R. BEIRNE, Esq.
18 Attorneys for the SEC

19 JAMES J. HAMMARH, pro se

2 THE COURT: Let us go on the record. Mr.
3 Hammarth, are you or are you not a member of the corporation,
4 stockholder or officer?

5 MR. HAMMARTH: I am not sir.

6 THE COURT: You are not.

7 MR. HAMMARTH: No, sir.

8 THE COURT: Do you have the books or records of
9 Midland Equity Corporation?

10 MR. HAMMARTH: No, sir.

11 THE COURT: None of them at all?

12 MR. HAMMARTH: No, sir.

13 THE COURT: Midland is not appearing here?

14 MR. HAMMARTH: No, sir.

15 MR. GREGG: Your Honor, according to the rules
16 of the Securities and Exchange Commission which regulate all
17 broker-dealers under section 15 (a), Mr. Hammarth is still
18 registered as a broker-dealer to the entity Midland Equity,
19 a New York corporation. Until such time as he is permitted
20 to withdraw by the Securities and Exchange Commission, he
21 remains a broker-dealer. If this were not so, any time a
22 broker-dealer had a violation which seriously or not seriously
23 affected the public interest, he could simply make the policy
24 and the enforcement posture of the Commission absurd by
25 saying, "I am no longer registered." This is not permitted.

2 I don't have a case at my fingertips, but I know
3 that there is a procedure, and I assure your Honor I will
4 brief the question, if necessary, that a registered broker-
5 dealer follow a procedure before he can be permitted to
6 withdraw.

7 We have requested on numerous occasions -- I don't
8 want to get involved in namecalling -- but we have attempted
9 to educate the defendant as to our policy.

10 MR. HAMMARTH: I object to that, your Honor.

11 MR. GREGG: I think the moving papers make out a
12 clear case of a position that we were forced into.

13 MR. HAMMARTH: Your Honor, I object to his giving
14 testimony without citation.

15 THE COURT: Wait. You will get a chance to
16 speak. Don't interrupt him.

17 MR. GREGG: In effect, your Honor, we were forced
18 into a posture where we had to appeal for the aid of a
19 federal court to enforce this law. We have, I feel, as the
20 cases indicate in this Circuit, specifically the case that
21 we briefed, Olsen, extended every courtesy to Mr. Hammarth.
22 It is a most basic provision of the securities law, section
23 17(a) -- it is not even a rule -- which says that a broker-
24 dealer must permit at any reasonable time and from time to
25 time inspection by officers of the Commission, staff members

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2 of the Commission. Therefore, whether Mr. Hammarth thinks
3 that Midland is registered at the present time or not, it is
4 in fact registered.

5 We are prepared to put on a witness if necessary
6 and present one exhibit that is the official file of the
7 Commission that indicates that Midland is still a broker-
8 dealer and that Mr. Hammarth is still president. Until such
9 time as the proper amendments are presented and the proper
10 procedures are followed, that remains the status quo.

11 Obviously, I would like to allude to one thing.
12 The scope of this injunction that we are requesting is
13 basically geared toward section 17(a) of the 1934 act, and
14 specifically to the inspection and visitation provisions.
15 And this is an extremely basic provision in the securities
16 law, for without our inspection and visitation power we
17 cannot determine if proper books and records are being kept,
18 if the net capital rule is being violated, and a whole series
19 of other rules that generally come under the term "securities
20 acts." If we are thwarted in this way, we cannot perform
21 our function as a public interest agency and we cannot
22 protect the public.

23 So we are appealing to the Court to give us the
24 relief that we request.

25 THE COURT: Yes, Mr. Hammarth.

2 MR. HAMMARTH: Your Honor, I think I covered
3 everything that Mr. Gregg said in my affidavit, in my judg-
4 ment, and I think I have covered it thoroughly, I have
5 documented it. I would like to let that statement that I
6 handed up stand, my affidavit to you. If you would like, I
7 will read it all.

8 THE COURT: There is no need to read it aloud.
9 I have it here.

10 MR. HAMMARTH: Further, I would like to, if I
11 could, make an unsworn editorial comment here. At any given
12 time, there were perhaps three, four thousand -- well, perhaps
13 3,700 registered broker-dealers in the United States, and
14 this is a matter of fact. About four or five guys a week
15 seem to get bilged out, which means, oh, in the course of a
16 year, depending on how bad the weather is, it's probably
17 300, 400, 500. In the course of a 10-year period, well, it's
18 probably a minimum of 3,000, which is pretty close to 60, 70
19 percent of the brokerage population. All the violations
20 are not -- you know, not all violations but a great many of
21 them are done after the fact, and there are a lot of things
22 that are imposed on people after the fact. And very often
23 when these impositions are made, there is some comment to it
24 in the newspaper, firms are gone, there is no opportunity to
25 retort. Service is made, you know, "I called you up and I

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2 made the service." And, of course, I put this in my
3 testimony. And here we are.

4 THE COURT: What do you propose here, Mr. Hammarth?
5 They want to look at the books and the records.

6 MR. HAMMARTH: No.

7 THE COURT: They want to look at the books and
8 the records of Midland Equity.

9 MR. HAMMARTH: I was just making an editorial
10 comment.

11 THE COURT: I know you are making an editorial
12 comment, but they want to look at the books and records
13 of Midland Equity.

14 MR. HAMMARTH: Well, sir, I do not have the books
15 and records.

16 THE COURT: You don't have them. Where are they?

17 MR. HAMMARTH: I sold the corporation, sir.

18 THE COURT: You sold the corporation.

19 MR. HAMMARTH: I negotiated the sale of the
20 corporation.

21 THE COURT: When did you do that?

22 MR. HAMMARTH: It's in the statement. February 15.

23 THE COURT: And you have had nothing to do with it
24 since then?

25 MR. HAMMARTH: That's correct, sir.

2
3 THE COURT: Under the law you are still there
until you are relieved, according to the SEC.

4 MR. HAMMARTH: Sir, if I may, he has not documented
5 that. That is an undocumented position.

6 THE COURT: It is not undocumented. It is right
7 here.

8 MR. HAMMARTH: No, sir. I am not registered. I
9 was never registered as a broker-dealer. The corporation was
10 registered as a broker-dealer. I was an employee of the
11 corporation and in fact was not a stockholder.

12 THE COURT: To whom was the stock of the corpora-
13 tion transferred?

14 MR. HAMMARTH: Well, I didn't come prepared to --

15 THE COURT: Do you know?

16 MR. HAMMARTH: I have no way of knowing who the
17 stock ultimately was transferred to, because I lost control
18 of the books when I sold it.

19 THE COURT: You must have known who you sold it
20 to and who you gave the books to in February.

21 MR. HAMMARTH: You asked me a different question.
22 You asked me who the stock was transferred to.

23 THE COURT: All right, whom did you transfer the
24 possession of the books and so forth to?

25 MR. HAMMARTH: I delivered the books.

2 THE COURT: Yes?

3 MR. HAMMARTH: Yes.

4 THE COURT: To whom?

5 MR. HAMMARTH: Joseph P. Goggins.

6 THE COURT: And you have not engaged in any
7 security transactions since February 15?

8 MR. HAMMARTH: That's correct, sir.

9 THE COURT: And you are not registered any place
10 to deal in securities?

11 MR. HAMMARTH: No, sir.

12 THE COURT: What are we going to do?

13 MR. GREGG: Your Honor, first of all, we would
14 like to ask that you take judicial notice of the official
15 file, broker-dealer file, of Midland Equity. It will
16 demonstrate that Mr. Hammarth is indeed still registered
17 pursuant to law.

18 THE COURT: All right.

19 MR. GREGG: As a second matter, Mr. Hammarth
20 according to this file never held any stock; his wife owned
21 stock. But that is off to the side. But I still would like
22 to request that you take judicial notice of this file.

23 It seems to me that the most important thing we
24 have right here and right now is that Mr. Hammarth, as the
25 president and so on, if you will observe the file, is all of

2 the officers in this particular corporation, is responsible
3 for maintaining and controlling the books and records. If
4 those books and records have been passed on elsewhere -- and
5 he gave us a name, Joseph Goggins -- we know nothing about
6 this. We have to know where they are. They have to be
7 opened to us. And we would request that they be opened to
8 us.

9 We, for example, at the present time have no
10 knowledge of the extent of exposure of public customers, any
11 free credit balances that are being held, and so on. I have
12 highly hearsay evidence that came to me that it is not sub-
13 stantial, but I cannot rely on this. I have to rely on the
14 original records. As the cases say, the SEC cannot be asked
15 to rely on a summary. The SEC must see the originals.

16 THE COURT: What do we do if he does not have
17 those records? What do we do then? I mean, as a practical
18 matter.

19 MR. GREGG: As a practical matter, as much as I
20 don't like to say it, your Honor, I somewhat doubt the fact
21 that he has in a bona fide sale sold a series of books and
22 records of a nonexistent shell to someone else. I think that
23 Mr. Hammarth is evading the jurisdiction, evading the power
24 of the Securities and Exchange Commission, and this is just
25 another attempt in a series of -- I shouldn't say attempts to

2 thwart -- but in a series of instances of his ignoring us.

3 Now, perhaps something can be worked out between
4 Mr. Hammarth and the Commission whereby we could secure the
5 books and records from somebody else. I don't know how this
6 can be worked out, but this has to be worked out through
7 mutual cooperation.

8 THE COURT: I know it has.

9 MR. GREGG: We haven't seen or spoken to Mr.
10 Hammarth since October 26, although a number of attempts have
11 been made, and that is contained in my affidavit and the
12 affidavit of one of the compliance examiners from the
13 Commission.

14 THE COURT: Do you want to try and work out some-
15 thing with them, Mr. Hammarth, or not? You don't want to have
16 an injunction issued publicly to you in the papers; is that
17 about the size of it?

18 MR. HAMMARTH: That's correct.

19 THE COURT: Why don't you see if you can work this
20 out with them? I will put this over for a short period of
21 time.

22 MR. HAMMARTH: Sir, I am really -- these fellows,
23 I have had --

24 THE COURT: Now --

25 MR. HAMMARTH: I have had experiences with them.

2 THE COURT: All right. But they have got a very
3 definite precise function to perform. The investing public
4 has got to be protected. The authority is given to them to
5 go through steps to do that. If you are willing to cooperate
6 with them, perhaps you can work something out with them. If
7 you are not, then I will take the case under advisement and
8 render a decision. It is as simple as that. I am giving you
9 the opportunity now, if you want to, to discuss this with
10 them and see whether you can work out something that is
11 agreeable to both sides.

12 MR. HAMMARTH: My only experience with the NASD
13 and the Exchange has been bad. As I indicated, I doubted Mr.
14 Gregg's good faith in pursuing this thing, I have documented
15 that position, and if I enter into an agreement with him, the
16 only thing I can ultimately do is lose. If he wants to make
17 some offer to me, that is fine. But I am not going to enter
18 into an agreement --

19 THE COURT: His offer here is to look at your
20 records and books and have them produced, in order to find out
21 what is going on.

22 MR. HAMMARTH: Sir, I cannot really do that. I
23 don't know where they are.

24 THE COURT: All right, then we may have to do
25 something else.

2 MR. GREGG: Judge, in any case whatever agreement
3 we work out we need our injunction for future violations of
4 17(a) and Rule 17(a) fraud. This is the way we proceed in an
5 enforcement posture.

6 MR. HAMMARTH: This is corruption of the blood.
7 What he really wants to do is to prevent me from ever being
8 in the securities business again, which is standard operating
9 procedure.

10 THE COURT: Your failure to cooperate may very
11 well result in that. Your cooperation might avoid that. I
12 don't know whether it will or not, but that is what you are
13 suggesting.

14 MR. HAMMARTH: As I said, if Mr. Gregg has some-
15 thing to offer, that is fine. But I have nothing to say.

16 MR. GREGG: Your Honor, I can't offer a deal
17 looking to the future on behalf of the Commission.

18 THE COURT: We don't have deals in the courthouse
19 anyhow.

20 MR. GREGG: I beg your Honor's pardon, I didn't
21 mean that.

22 THE COURT: I know you didn't mean it that way.

23 MR. GREGG: A compromise.

24 THE COURT: I am not going to be a party to that.

25 If you gentlemen can go outside and agree on something between

2 yourselves, do it. If you cannot, and I have to pass upon
3 this and you want to present that file, I will take it,
4 anything else you want to present I will take, and render a
5 decision. It is as easy as that. If testimony is to be
6 taken, we will take it.

7 MR. HAMMARTH: I would just as soon have a hearing
8 on the matter, because I don't have anything to say to him,
9 really.

10 THE COURT: All right.

11 MR. GREGG: Shall we proceed, your Honor?

12 THE COURT: You might just as well proceed,
13 certainly.

14 MR. GREGG: My name is Michael T. Gregg, for the
15 Securities and Exchange Commission, New York Regional Office.

16 MR. BEIRNE: Thomas R. Beirne, also for the
17 Securities and Exchange Commission.

18 MR. HAMMARTH: James J. Hammarth.

19 MR. GREGG: Your Honor, I am not going to make an
20 opening statement, obviously; we have exhausted that. I would
21 like to ask the clerk to mark the broker-dealer file for
22 identification, please.

23 (Plaintiff's Exhibit 1 marked for identification.)

24 MR. GREGG: Your Honor, I would like to call as
25 a witness Mr. George Appoldt of the Securities and Exchange

1 WC

Appoldt - direct

14

2 Commission.

3 G E O R G E C. A P P O L D T, called as a witness by
4 the plaintiff, being first duly sworn, testified as
5 follows:

6 DIRECT EXAMINATION

7 BY MR. GREGG:

8 Q Mr. Appoldt, are you employed?

9 A Yes, I am.

10 Q And, if so, where?

11 A With the SEcurities and Exchange Commission, New
12 York Regional Office.

13 Q What is your title, sir?

14 A I am a securities compliance examiner.

15 Q Would you please give me a brief description of
16 your duties.

17 A Well, we go in to look at the books and records
18 of broker-dealers. We also work with the attorneys taking
19 testimony and preparing affidavits of things we have done on
20 cases. We also have a lot of new men over there, inexperienced,
21 and I have taken those out on jobs with me.

22 Q When you say "jobs," do you mean inspections?

23 A Inspections.

24 Q Broker-dealers?

25 A Right.

1 wc

Appoldt - direct

2 Q How long have you been so employed?

3 A I have been with the Commission since July of
4 1972.5 Q Previous to your employment with the Commission
6 did you work in the securities industry?

7 A Yes, I did, for nineteen years.

8 Q In what aspect of the securities industry?

9 A I worked in what is known as the back office, the
10 cashier's department, which handled money, securities, and
11 books and records.12 Q Will you please give me, Mr. Appoldt, a short
13 description of your previous employment.14 A Yes. Well, for a year prior to the Commission
15 I worked for a SIPC trustee -- that is Securities Investors
16 Protection Corporation. Before that, I worked with a
17 brokerage firm named Baron & Company.

18 Q What did you do at Baron?

19 A I was cashier at Baron & Company.

20 Q Were you in a supervisory capacity?

21 A Yes, I was.

22 Q Is that a supervisory job?

23 A Yes, it is. I was in charge of, as I said, the
24 back office.

25 Q Thank you.

2 A Prior to that I was twelve years with Pershing &
3 Company, who are members of the New York Stock Exchange. I
4 started out there as a stock delivery clerk and finished there
5 as cashier, again in a supervisory position.

6 Q Did there come a time in the course of your
7 official duties as compliance examiner at the SEC when you
8 were called upon to visit the firm of Midland Equity?

9 A Yes. There was. I received an inspection
10 assignment from the chief of our branch, broker-dealer branch,
11 to go down and look at the books and records of Midland
12 Equity.

13 Q How did you ascertain the address of Midland
14 Equities?

15 A Well, with the broker-dealer file, which is known
16 as the No. 1 file; I believe you have that in your hand right
17 now.

18 Q I now show you what is marked as Commission's
19 Exhibit 1 for identification and ask you if that is that file.

20 A Yes, this is the ED-1 file. This file contains
21 general information about a brokerage house; each brokerage
22 house in the New York - New Jersey area has a file such as
23 this at the Commission. It also lists people who are
24 principals or officers of the company or corporation and gives
25 a financial picture of the company when it first goes in to

25

2 operation.

3 Q I take it that it is your testimony that from
4 this file, from this 1 file, you found out the address of
5 Midland Equity?

6 A Yes.

7 Q Did you in fact proceed to the offices of Midland
8 Equity?

9 A Yes, we did. That was at 160 Broadway. That was
10 sometime late in October of '72. Another compliance examiner,
11 Robert Green, G-r-e-e-n, and myself went out to look at the
12 books and records of Midland Equity. Upon getting to the
13 building, we looked at the building directory and saw that the
14 room number was 1102. We proceeded to Room 1102, found the
15 door to be locked. Another name, not Midland Equity, was on
16 the door. Knocked at the door, tried the handle, and I think
17 we may have even peeked in the mail slot in the door to see if
18 anyone was inside. And it appeared to be that the room was
19 empty.

20 We then went downstairs to the building manager
21 and found out that Room 1102 is occupied by an answering
22 service.

23 From there Mr. Green and I proceeded to a
24 certified public accountant named Bach, B-a-c-h, who --

25 Q Was this on the same day?

1 WC

Appoldt - direct

18

2 A Yes.

3 Q Yes.

4 A Who according to, again, the broker-dealer file
5 had done the last financial audit, independent audit on
6 Midland Equity. He was located on 50 Broadway. Being that
7 he was in the area, we walked down. We spoke to Mr. Bach and
8 found out that Mr. Hammarth could be found in Room 910 at 160
9 Broadway. He was sharing the office with someone else, as
10 Mr. Bach had told us. We then went back to 160 Broadway,
11 Room 910, and the door was locked. We tried again and tried
12 the knob, knocked, got no reply, and so we returned to our
13 office.

14 The next morning at approximately 10, 10:30, Mr.
15 Green and I again went to 160 Broadway, went to Room 910,
16 where we found the door slightly ajar. We knocked, walked in.
17 A gentleman was seated there. We asked him if Mr. Hammarth
18 was there. He said he wasn't, but he might be available if
19 we identified ourselves, or words to that effect. We then
20 identified ourselves as being from the Commission, and the
21 gentleman I took to be Mr. Hammarth said, "Well, what do you
22 want?" We said, "We want to look at the -- inspect the
23 books and records." And he said again words to the effect of
24 "Well, I didn't show them to NASD and I won't show them to
25 you." I asked him why, and he said he was no longer a member

2 A Yes.

3 Q Yes.

4 A Who according to, again, the broker-dealer file
5 had done the last financial audit, independent audit on
6 Midland Equity. He was located on 50 Broadway. Being that
7 he was in the area, we walked down. We spoke to Mr. Bach and
8 found out that Mr. Hammarth could be found in Room 910 at 160
9 Broadway. He was sharing the office with someone else, as
10 Mr. Bach had told us. We then went back to 160 Broadway,
11 Room 910, and the door was locked. We tried again and tried
12 the knob, knocked, got no reply, and so we returned to our
13 office.

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15 Green and I again went to 160 Broadway, went to Room 910,
16 where we found the door slightly ajar. We knocked, walked in.
17 A gentleman was seated there. We asked him if Mr. Hammarth
18 was there. He said he wasn't, but he might be available if
19 we identified ourselves, or words to that effect. We then
20 identified ourselves as being from the Commission, and the
21 gentleman I took to be Mr. Hammarth said, "Well, what do you
22 want?" We said, "We want to look at the -- inspect the
23 books and records." And he said again words to the effect of
24 "Well, I didn't show them to NASD and I won't show them to
25 you." I asked him why, and he said he was no longer a member

1 WC

Appoldt - direct

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2 of the NASD or the SEC.

3 I asked him what he based his reasoning on, and
4 he gave me a copy of a letter that he had received.

5 MR. GREGG: I would ask that the clerk mark
6 this letter as Commission's Exhibit No. 2 for identification.

7 (Plaintiff's Exhibit 2 marked for identification.)

8 Q Mr. Appoldt, I would ask you first, is the
9 gentleman that you met that October day, you said, some day
10 in October --

11 A Yes.

12 Q -- is he in the courtroom right now?

13 A Yes. He is sitting right at the table here.

14 Q That is Mr. Hammarth, the defendant. Thank you.
15 You spoke of a letter, and I show you what has been marked
16 as Plaintiff's Exhibit No. 2 for identification.

17 A Yes.

18 Q Is that the letter?

19 A This is a copy, yes, that Mr Hammarth in fact
20 made for us while we were at his office, and he brought my
21 attention to paragraph (A), which in more or less general
22 terms says that if you don't pay the SIPC assessment --

23 - Q You don't have to paraphrase it.

24 A OK.

25 Q It is in evidence.

A And he said that was the reason he was no longer a broker-dealer. I then asked him if he was doing any business at the time, and he said no. I asked him also if he would send us a letter to the effect that he was doing no business. And he said yes. At which time we shook hands and I said, "Thank you," and we left the office.

When I got back to the office, I then wrote a memorandum to William Nortman, who is the Assistant Regional Administrator of the Commission, outlining everything I had just said here as to what happened during the course of our investigation or trying to investigate, look into the books and records of Midland. And up until this time, I don't believe, I have never seen or found, a letter.

Q Have you checked?

A Yes. In, again, the files of Midland Equity.

Q Such a letter, if received, would be --

A Would be in the files, yes.

MR. GREGG: At this time, your Honor, I would like to move the admission of Plaintiff's Exhibits 1 and 2 into evidence.

THE COURT: Show them to Mr. Hammarth.

VOIR DIRE EXAMINATION

BY MR. HAMMARTH:

Q Mr. Appoldt, you received the letter in my office,

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1 WC

Appoldt - direct

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2 I assume?

3 A Yes, sir.

4 Q Did you ever make any further comment on that
5 letter in writing or orally to my office?

6 A I believe that I called you up and asked you
7 again, perhaps it was later that afternoon or the next day, if
8 you would send us a letter saying that you were no longer
9 doing business.

10 Q Sir, I asked you if you made any comment as to
11 that letter that I had given you?

12 A After I read the paragraph, I asked you what you
13 were trying to tell me or what you were trying to get across,
14 as I remember --

15 Q After you left the office, did you call at my
16 office, write me a letter, or communicate with me in any way
17 regarding the possible consequences of that paragraph?

18 A Not that I remember, sir.

19 MR. HAMMARTH: Thank you very much, Mr. Appoldt.

20 THE COURT: Any objection to this being marked
21 in evidence?

22 MR. HAMMARTH: Pardon me?

23 THE COURT: Any objection to the letter in
24 Exhibit 1?

25 MR. HAMMARTH: Oh, no, sir.

2 THE COURT: It will be received in evidence.
3 (Plaintiff's Exhibits 1 and 2 received in
4 evidence.)

5 MR. GREGG: Thank you. I have no further
6 questions of Mr. Appoldt.

7 THE COURT: Any questions of Mr. Appoldt, Mr.
8 Hammarth?

9 MR. HAMMARTH: No, sir.

10 THE COURT: All right.

11 (Witness excused)

12 THE COURT: Anything further, Mr. Gregg?

13 MR. GREGG: One moment, please, your Honor.

14 Your Honor, perhaps I have a suggestion to make
15 which may save some time. With respect to the activities that
16 took place, principally by me, after Mr. Appoldt's visit to
17 Midland, in a scanning of the affidavit it appears that Mr.
18 Hammarth does not contest the fact that they were made or that
19 further attempts were made. If perhaps we could have a
20 stipulation to that at this time, it might clarify at least
21 some of the issues in this matter.

22 MR. HAMMARTH: No. I would rather get Mr. whatever-
23 his-name, Mr. Gregg's testimony.

24

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2 M I C H A E L T. G R E G G, called as a witness by
3 the plaintiff, being first duly sworn, testified as
4 follows:

5 DIRECT EXAMINATION

6 BY MR. BEIRNE:

7 Q Are you employed, Mr. Gregg?

8 A Yes, I am.

9 Q Where do you work?

10 A I work for the Securities and Exchange Commission,
11 Division of Enforcement, New York Regional Office.

12 Q Will you briefly describe your duties as an
13 enforcement attorney?

14 A As an enforcement attorney, I receive from my
15 legal superiors, that is, my attorney superiors, various
16 tasks with a view towards investigating and, if necessary,
17 drafting court papers and so on, generally with a view
18 towards enforcing the securities laws.

19 Q From time to time are you assigned to investigate
20 certain broker-dealers as far as possible violations are
21 concerned?

22 A Yes, I am.

23 THE COURT: Why don't you just tell us what
24 relationships you had with Midland and Hammarth. All right?

25 A After Mr. Appoldt's return to the office and

informing of his superiors, I would say about six weeks thereafter I received an assignment from my ultimate superior in enforcement, which is William Nortman, to look into the matter of Midland Equity, to determine if in fact a broker-dealer had refused to allow the Commission to observe their books, that is, inspect his books. This would be some time in November of '72, I would say late November.

At that time I began to call the telephone number listed for Midland Equity and leave a series of messages for Mr. Hammarth, in the hopes that we could arrange some settlement of this problem that we appeared to be having. Mr. Hammarth returned my call on some day in December, I would say mid-December 1972, whereupon I outlined what our problem was with him and requested that he permit the compliance examiners to inspect the books and records.

Mr. Hammarth indicated that substantially the same argument he indicated to me that he had given to the compliance examiner Appoldt, that I believe it was section 10(a) of the Securities Investor Protection Act, which when a broker-dealer who is registered does not pay his SIPC assessment -- SIPC is the acronym for Securities Investor Protection Corporation -- when he does not pay his assessment, he is prohibited by the SIPC Act of 1970 from engaging in a business as a broker-dealer.

2 Mr. Hammarth directed my attention to that
3 provision, and I read it while I was on the phone with him,
4 and said to him, "Yes, I agree that you are not prohibited.
5 Nonetheless, this does not change the provisions of the 1934
6 act, section 17(a), which indicates the inspection problem.

7 Mr. Hammarth told me that he didn't agree with me,
8 and then I explained to Mr. Hammarth that it's possible that
9 an enforcement action would be brought based upon this.

10 This matter was shunted aside because of other
11 more pressing workload considerations. Sometime in January
12 I contacted NASD, which is the National Association of
13 Securities Dealers, and they indicated to me that they had
14 the same problem with Mr. Hammarth and Midland Equity, but
15 they would not produce various information that they had
16 gleaned without a subpoena. They did inform me that he had
17 certain customer accounts, or at least they felt that he did.
18 Whereupon around the end of January I wrote a letter to Mr.
19 Hammarth indicating substantially the same -- repeating the
20 demand.

21 Between the time the letter was written at the end
22 of January until the filing of the complaint in this matter,
23 I would estimate that I called premises of Midland Equity two
24 times to renew the demand, never having spoken to Mr. Hammarth
25 except for that first time and never having received a return.

2 call.

3 Eventually, in the course of my duties, I
4 requested authority from the Commission with the approval of
5 my superiors to file an injunctive action.

6 Q Did you also attempt to contact Mr. Hammarth with
7 respect to the pendency of this proceeding?

8 A Yes, I did.

9 Q Were you successful in reaching him?

10 A No, I was not. I called at his place of business
11 a couple of times at each stage in the early part of this.
12 the filing of the complaint, when we were approaching his
13 Honor for a TRO and so on, leaving messages to that effect at
14 his place of business, which I take it is an answering service.
15 I also called his number listed at his former address, and on
16 the second call—I discovered on both calls that he had moved,
17 but the second time I called I was informed of his ~~new~~
18 address. And at that time I didn't attempt to contact him
19 at his new address, because the TRO had already been signed.

20 Q Then did you instruct someone to serve the papers?

21 A Yes, I did.

22 MR. BEIRNE: No further questions.

23 THE COURT: All right, Mr. Hammarth.

24

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1 WC

Gregg - cross

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2 CROSS EXAMINATION

3 BY MR. HAMMARTH:

4 Q Mr. Gregg, if a member of SIPC doesn't pay his
5 dues and he is a member of the stock exchange, what happens?
6 Does he have any further opportunity to operate under the
7 authority of the New York Stock Exchange?

8 MR. BEIRNE: Your Honor, I submit this is a legal
9 question.

10 MR. HAMMARTH: Sir, it is not a legal question at
11 all. It is right in my reference, Exhibit 2. The answer is
12 right there for you to read.

13 THE COURT: You know the answer to that, Mr.
14 Gregg?

15 A I am not quite sure I understand the question.
16 Will you please repeat the question.

17 Q Should a member of the stock exchange not pay his
18 SIPC dues, could he operate any further? What happens to his
19 operation?

20 A I don't know the answer to that question, the New
21 York Stock Exchange.

22 MR. HAMMARTH: Sir, I would like to reference my
23 Exhibit 1 and 2.

24 Q If a member of any other securities exchange does
25 not pay his SIPC assessment, what happens?

2 A I can answer you generally, if a member of a
3 national securities association as it is defined --

4 Q Exchange, sir.

5 A Exchange?

6 Q Exchange.

7 A I don't know.

8 MR. HAMMARTH: Very well, sir. I would like to
9 reference my exhibit on that too.

10 Q If a member of the National Association of
11 Securities Dealers doesn't pay his SIPC dues, what happens?

12 THE COURT: How is this relevant to the issues we
13 have here?

14 MR. HAMMARTH: Well, sir, is this a serious
15 matter?

16 THE COURT: Serious matter or not --

17 Q Did you ever communicate with me in any official
18 way about the effect of SIPC on my operation when I inter-
19 posed that objection?

20 A Any time I called a broker-dealer it's an official
21 call, because it's in the course of my business. Therefore,
22 I would say, No. 1, the telephone call that you returned to
23 me, when we discussed this, the first time, and then, No. 2,
24 the letter that I wrote to you, indicating the problems that
25 could result from a failure to permit inspection, fall within

1 wc

Gregg - cross

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2 the scope of your question, yes.

3 Q Sir, have you thoroughly acquainted yourself
4 with SIPC regulations?

5 A No. I am not a SIPC expert by any means.

6 Q Mr. Gregg, you said you composed a letter to me
7 on the 31st of January, 1973, is that correct?

8 A Yes, I did.

9 Q Sir, is there any indication in that letter when
10 you are going to inspect?

11 A No.

12 Q Is there any suggested course of action in that
13 letter?

14 A There is a cause of action implicit in it: refusal
15 to permit inspection.

16 Q Is there any suggested course of action in the
17 letter?

18 A Yes, the suggested course of action is that you
19 call me --

20 Q Sir, is there any suggested course of action in
21 that letter?

22 MR. BEIRNE: Your Honor, may the witness be
23 allowed to answer the question.

24 THE COURT: Yes, let him answer the question.

25 A The course of action proposed to you is to call the

2 attorney assigned to the matter and arrange for an inspection
3 of your books and records.

4 Q How would you in that instance differentiate
5 between an informational sentence and a suggested course of
6 action?

7 A May I see the letter?

8 Q Certainly (handing to the witness).

9 MR. BEIRNE: Your Honor, I don't think that last
10 question is relevant or even comprehensible.

11 THE COURT: The letter speaks for itself.

12 A If I may, to answer it simply, the purpose of the
13 letter is to renew the demand of the office, which the office
14 has power to renew.

15 MR. HAMMARTH: After the letter, we have a large
16 vacant area and we don't hear from Mr. Gregg again until
17 June, I think.

18 Q Mr. Gregg, in what fashion were you pursuing
19 this situation in the intervening period of time, which is
20 three and a half months?

21 A I was pursuing it very lightly. I had various
22 other matters which occupied my time completely.

23 Q Would you agree that a temporary restraining
24 order and order to show cause is a serious imposition of
25 penalty?

2 A It's a drastic remedy, but we have a drastic
3 situation here. That is why the relief was requested.

4 Q What in the situation in that period of time
5 changed the situation that caused you to apply for the most
6 drastic remedy you could get under the circumstances?

7 MR. BEIRNE: Your Honor, I object.

8 THE COURT: Yes. All I can suggest to you, Mr.
9 Hammarth, is that I gave you the opportunity. If you want
10 to discuss it with him now to see what you could work out
11 with him, you may. But it does not seem to be acceptable.
12 That is why we have this matter here now.

13 X THE WITNESS: Your Honor, with respect to that --

14 THE COURT: You don't have to answer it. The
15 fact is whether he is delayed or not does not make any
16 difference on the question of the application of the temporary
17 restraining order. The question here is, are you in violation?
18 If you are in violation, what kind of action am I going to
19 take thereon? The fact that he may have delayed in getting it
20 does not go to the question of the right to get this remedy.

21 Do you have anything further?

22 MR. HAMMARTH: No, sir.

23 THE COURT: Anything further?

24 THE WITNESS: No.

25 (Witness excused)

2 THE COURT: Do you want to present anything,
3 Mr. Hammarth? You have submitted your affidavit, which I
4 have.

5 MR. HAMMARTH: I will rest on that, sir.

6 THE COURT: You rest on that. All right. Are you
7 going to get the transcript here, Mr. Gregg?

8 MR. GREGG: Yes.

9 THE COURT: And submit.

10 MR. GREGG: We will fully brief the question.

11 THE COURT: When will you brief the question?

12 Today is Thursday. I would suggest that a week from Monday
13 you will have.

14 MR. GREGG: I will work on the legal aspect first.

15 THE COURT: And if it takes a little longer to
16 get the minutes, you can call and I will give an extension of
17 time. Serve Mr. Hammarth with a copy of your post-findings
18 and your brief.

19 Do you want any time to respond to that, Mr.
20 Hammarth?

21 MR. HAMMARTH: Pardon me, sir?

22 THE COURT: Do you want time to respond?

23 MR. HAMMARTH: How much time to respond to which?

24 THE COURT: I am asking them to submit a
25 memorandum of law and proposed findings in this matter by a

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2 week from Monday, which would be July 2.

3 MR. HAMMARTH: Sir, if we could make it the week
4 after the 4th.

5 THE COURT: All right, if you have it on July 2,
6 then you have a response to them on July 9. Do you know
7 where to serve them or send the papers to them?

8 MR. GREGG: Now I do, your Honor.

9 THE COURT: You do know. By mail is sufficient.

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